Financial Management and Internal Controls at Selected Agencies – Interior Transportation, Homeland Security, and Defense

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Internal Control References

- DoD Website: http://www.dod.mil/comptroller/fmfia/index.html
- Federal Managers' Financial Integrity Act of 1982 (PL 97-255)
- OMB Circular A-123, Management's Responsibility for Internal Control, August 5, 2005 (Recently revised)
- DoD Directive 5010.38, Management Control Program, 26 August 1996 – (Under revision)
- DoD Instruction 5010.40, Management Control Program Procedures, 28 August 1999 (Under revision)
- Guidelines for Preparation of the Federal Managers' Financial Integrity Act Annual Assurance Statement – November 8, 2005
- GAO Standards for Internal Control in the Federal Government, November 1999

Agenda

- **Who We Are**
- **What We Do**
- **Our Awareness Challenge**
- **DoD FY 2005 Statement of Assurance Improvement**
- **DoD Scorecard**
- **Summary**
- **FY 2006 Scorecard Criteria (BACKUP)**

Department of Defense -- Who Are We?

PEOPLE

- **3 Million people stationed in 146 countries**
  - **1.4 million active duty men and women**
  - **1.2 million Guard and Reserve**
  - **654,000 civilians**
  - **2 million retirees and families receive benefits**

INFRASTRUCTURE

- **600,000 buildings /structures in over 6,000 locations on more than 30 million acres of land in 146 countries**

PLANT, PROPERTY AND EQUIPMENT

- **250,000 vehicles**
- **15,000 aircraft**
- **1,000 oceangoing vessels**

Department of Defense -- Who Are We? (cont)

<u>ORGANIZATION</u>:

- **4 Military Services (Army, Air Force, Navy and Marines)**
- **9 Combatant Commands**
  - **European Command**
  - **Central Command**
  - **Pacific Command**
  - **Northern Command**
  - **Strategic Command**
  - **Special Operations Command**
  - **Transportation Command**
  - **Joint Forces Command**
- **Office of the Secretary of Defense and DoD Field Activities**
- **Office of the Chairman of the Joint Chiefs of Staff**

Department of Defense -- Who Are We? (cont)

ORGANIZATION (continued):

- **17 DoD Agencies**
  - **Defense Advanced Research Projects Agency (1958)**
  - **Defense Business Transformation Agency (2003)**
  - **Defense Commissary Agency (1990)**
  - **Defense Contract Audit Agency (1965)**
  - **Defense Contract Management Agency (2000)**
  - **Defense Finance and Accounting Agency (1990)**
  - **Defense Information Systems Agency (1960)**
  - **Defense Intelligence Agency ((1961)**
  - **Defense Legal Services Agency (1981)**
  - **Defense Logistics Agency (1961)**
  - **Defense Security Cooperation Agency (1971)**
  - **Defense Security Agency (1972)**
  - **Defense Threat Reduction Agency (1959)**
  - **Missile Defense Agency (1984)**
  - **National Geospatial-Intelligence Agency (1972)**
  - **National Security Agency / Central Security Service (1952)**
  - **Pentagon Force Protection Agency (2002)**

Department of Defense – What We Do?

- Defend the United States
- Deter aggression and coercion
- Swiftly defeat aggression
- Conduct smaller-scale contingency operations

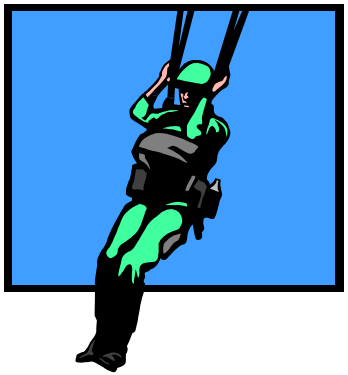
Department of Defense -- What We Do? (cont)

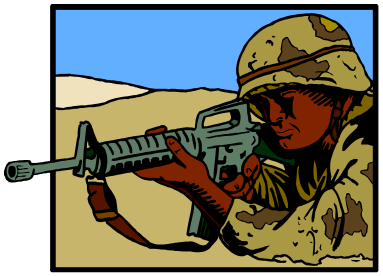
Examples of the Volume of Our Business

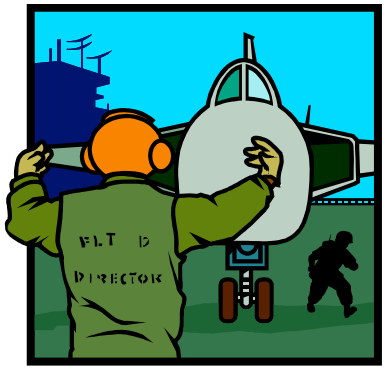
- **Defense Logistics Agency:**
  - **54,000 requisitions a day**
  - **8,200 contracts a day**
  - **26 distribution depots**
  - **24.7 million annual receipts and issues**
  - **132.8 million barrels of fuel sold**

- **Defense Finance and Accounting Service:**
  - **104 million pay transactions for 5.9 million people**
  - **6.9 million travel payments**
  - **12.6 million commercial invoices**
  - **127.3 million general ledger transactions**
  - **$234 billion managed military retirement and health benefits funds**
  - **$455 billion in annual disbursements to pay recipients**
  - **$13.5 billion in foreign military sales**

The Nature of Our Work Demands That We…..
<u>Be in Control</u>!!

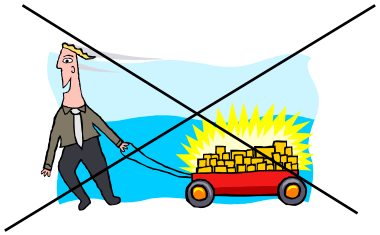






Because of what can happen…
When Things Are Out of Control?

Many Types of Jobs Require Many Kinds of Controls



Separation of duties

Chemical gloves

Reconciliation

Military Example

Mission Objective: Obtain proficiency in parachuting with

Possible Risk: Parachute fails to open properly due to incorrect rigging.

Internal Control Activity: Final jumpmaster safety inspect parachute rigging.

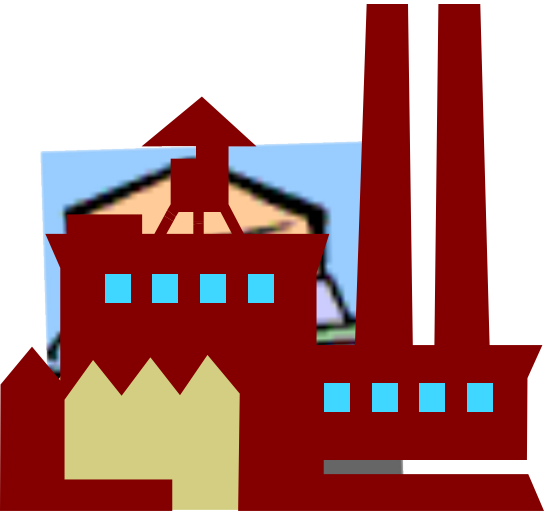
Not Just a Financial Requirement --

Ranger Training

Four died **Hypothermia**

Ineffective Internal Controls on Safety

Can Affect Both Operations and Financial At the Same Time



Factory

Foxhole

Operational Concern

- Inadequate supply quantities to meet deployed forces needs (certain items)
- Inadequate management of shipping containers
- Inadequate protection at the distribution centers causing pilferage
- Inadequate visibility over equipment / supplies transported from factory to foxhole

Financial Statement Concern

- Inability to properly value inventory on financial statements

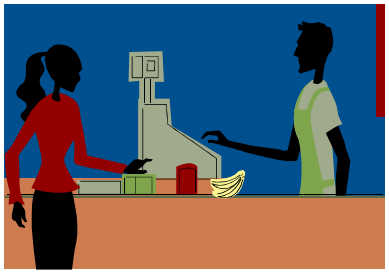
How Do We Increase Awareness????

Public Relations (PR) Campaign

- DoD is developing a PR Campaign:
  - Raise awareness on the importance of effective internal controls
- Target Audience:
  - DoD Leadership:
    - Senior Civilian and Military Leaders
    - DoD Managers and Supervisors
  - DoD Managers' Internal Control Program Coordinators
  - All DoD Personnel
- Key Themes:
  - Defense needs better awareness to help reduce situations where you have to ask, "How could that have happened?"
  - Leadership is ultimately responsible, but all personnel must help
  - Senior leadership must demonstrate commitment
  - Training is essential
- Strategy:
  - Develop slogan – Defense-wide contest…..
  - Develop ways to communicate our message with universal appeal

Need assistance to raise awareness at Components

DoD Scorecard



Statement of Assurance Scorecard… Why Score?

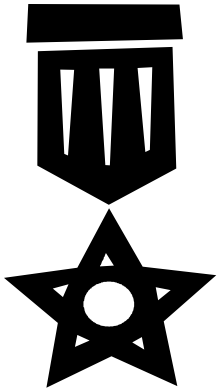
- Began in FY 2003
- Help improve DoD Components' reporting performance in five categories – And it's working!!
- Provide constructive feedback to Components
- Recognize top performers
- Improve timeliness so DoD can prepare and report on time

Five Scorecard Categories… What Scored?

- Timeliness (points for early and timely reporting)
- Format (points for well-written reports requiring no revision)
  - Accurate, complete, easy to read
  - Compliance with Directive, Instruction, and Annual Guidance
  - No revisions required because revisions risk timely reporting
- Component-wide program execution (points for evidence of methods used to improve program execution)
- Component-wide training (points for evidence of different types of training and to whom)
- Material weakness reporting (points for prompt resolution of weaknesses and evidence that assessments were conducted)
  - Percentage of weaknesses corrected on time
  - If no weaknesses reported, evidence of robust assessment used

Scorecard…
Components Receiving High Scores

- First Place
  - Defense Logistics Agency
  - Department of the Air Force
  - Department of the Navy
- Second Place
  - Defense Finance and Accounting Service
- Third Place
  - Defense Commissary Agency
  - Defense Intelligence Agency
  - Pentagon Force Protection Agency
  - US Special Operations Command
- Fourth Place
  - National Defense University
  - National Security Agency
  - Office of the Secretary of Defense (Consolidated Statement)
  - US Pacific Command
  - US Strategic Command



Scorecard Total Results

Agency	Timely	Format	Program Execution	Training	Material Weaknesses Reporting	FY 2005 Color Score	FY 2005 Overall Score	Change from FY 2004 Overall Score
Defense Logistics Agency	Green	Blue	Blue	Blue	White	Blue	3.2	+1.6
Department of Air Force	Green	Blue	Blue	Blue	White	Blue	3.2	+0.4
Department of Navy	Green	Blue	Blue	Blue	White	Blue	3.2	+1.4
Defense Finance and Accounting Service	Green	Blue	Blue	Green	White	Blue	3.0	+1.6
Defense Commissary Agency	Blue	Blue	Blue	Blue	Green	Green	2.8	+0.2
Defense Intelligence								

Point Values: White = 5, Purple = 4, Blue = 3, Green = 2, Amber = 1, and Red = -1

Scorecard Total Results (Cont)

Agency	Timely	Format	Program Execution	Training	Material Weakness Reporting	FY 2005 Color Score	FY 2005 Overall Score	Change from FY 2004 Overall Score
Pentagon Force Protection Agency	Blue	Blue	Blue	Blue	Green	Green	2.8	+0.4
US Special Operations Command	Blue	Blue	Blue	Blue	Green	Green	2.8	+0.2
National Defense University	Blue	Green	Blue	Blue	Green	Green	2.6	+0.8
National Security Agency	Green	Blue	Blue	Blue	Green	Green	2.6	0.0
Office of the Secretary of Defense, Consolidated Principal Staff & Field Activities	Green	Blue	Blue	Blue	Green	Green	2.6	-0.2

Point Values: White = 5, Purple = 4, Blue = 3, Green = 2, Amber = 1, and Red =

Scorecard Total Results (Cont)

Agency	Timely	Format	Program Execution	Training	Material Weaknesses Reporting	FY 2005 Color Score	FY 2005 Overall Score	Change from FY 2004 Overall Score
US Pacific Command	Blue	Green	Green	Green	Purple	Green	2.6	+1.6
US Strategic Commend	Blue	Green	Blue	Blue	Green	Green	2.6	+0.4
Defense Information Systems Agency	Green	Green	Blue	Blue	Green	Green	2.4	+0.6
Defense Security Cooperation Agency	Blue	Amber	Green	Green	Purple	Green	2.4	+.1.0
Joint Staff	Green	Blue	Green	Blue	Green	Green	2.4	0.0
Missile Defense Agency	Green	Green	Blue	Blue	Green	Green	2.4	0.0

Point Values: White = 5, Purple = 4, Blue = 3, Green = 2, Amber = 1, and Red = -1

Scorecard Total Results (Cont)

Agency	Timely	Format	Program Execution	Training	Material Weaknesses Reporting	FY 2005 Color Score	FY 2005 Overall Score	Change from FY 2004 Overall Score
National Geo-Spatial Intelligence Agency	Blue	Green	Blue	Green	Green	Green	2.4	+0.4
Inspector General	Blue	Green	Blue	Green	Green	Green	2.4	+1.0
US Southern Command	Blue	Green	Green	Blue	Green	Green	2.4	+0.2
US Transportation Command	Green	Green	Blue	Blue	Green	Green	2.4	+0.6
Defense Advanced Research Projects Agency	Blue	Blue	Green	Green	Amber	Green	2.2	0.0

Point Values: White = 5, Purple = 4, Blue = 3, Green = 2, Amber = 1, and Red = -1

Scorecard Total Results (Cont)

Agency	Timely	Format	Program Execution	Training	Material Weaknesses Reporting	FY 2005 Color Score	FY 2005 Overall Score	Change from FY 2004 Overall Score
Defense Contract Audit Agency	Blue	Green	Green	Green	Green	Green	2.2	+0.4
Uniformed Service University of the Health Sciences	Blue	Green	Green	Green	Green	Green	2.2	+0.4
Defense Contract Management Agency	Blue	Green	Green	Green	Amber	Green	2.0	+0.8
Defense Threat Reduction Agency	Green	Green	Green	Green	Green	Green	2.0	+0.6

Point Values: White = 5, Purple = 4, Blue = 3, Green = 2, Amber = 1, and Red = -1

Scorecard Total Results (Cont)

Agency	Timely	Format	Program Execution	Training	Material Weakness Reporting	FY 2005 Color Score	FY 2005 Overall Score	Change from FY 2004 Overall Score
US Central Command	Green	Green	Green	Green	Green	Green	2.0	+1.6
US Joint Forces Command	Blue	Green	Green	Green	Amber	Green	2.0	+1.0
US Northern Command	Green	Green	Green	Green	Green	Green	2.0	+0.6
Defense Security Service	Green	Amber	Green	Red	White	Amber	1.8	+1.0
US European Command	Green	Green	Green	Amber	Green	Amber	1.8	+1.6
Department of the Army	Red	Green	Amber	Blue	Red	Red	0.8	-0.4

Point Values: White = 5, Purple = 4, Blue = 3, Green = 2, Amber = 1, and Red = -1

FY 2005 Statement of Assurance Improvements

Red = Unacceptable
Amber = Needs improvement
Green = Acceptable
Blue, Purple & White = Exceptional (receiving extra credit) points

- Percentage On Time:
  - 97% in FY 2005 (31 of 32)
  - 88% in FY 2004 (30 of 34)
  - 48% in FY 2003 (15 of 31)
- Percentage 7 days ahead of Suspense:
  - 50% in FY 2005 (16 of 32)
  - 18% in FY 2004 (6 of 34)
  - 10% in FY 2003 (3 of 31)
- Percentage of Weaknesses Completed:
  - 48% in FY 2005 (22 of 46)
  - 28% in FY 2004 (11 of 40)
  - 36% in FY 2003 (25 of 70)
- Eight of 10 delinquent weaknesses resolved

Delinquent Weakness Defined As:

- **Identified in FY 2000 or before, <u>and</u>**
- **Correction target date slipped more than twice, <u>and</u>**
- **Target date slipped 3 years past original target date**

DoD FY 2005 Statement of Assurance

Federal Managers' Financial Integrity Act (FMFIA)
Applies to All Programs and Operations

Managers will:

- Establish an effective system of internal controls
- Assess the effectiveness of internal controls
- Annually report assurance
  - Identifying material weaknesses
  - Describing plan and schedule for correcting

- (Unqualified) – "reasonable assurance that management (internal controls) are in place, effective, and being used."
- (Qualified) – "reasonable assurance that management (internal) controls are in place, effective, and being used except for…"
- (No Assurance) – "does not provide reasonable assurance."

Results FY 2005
Material and Systemic Weaknesses

- **Significantly Improved – Reduced 47 FMFIA weaknesses to 34**
- **<u>Overall Weaknesses in Internal Controls (Section 2)</u>**
  - **46 Weaknesses Beginning of FY 2005**
    - **22 Corrected (22 Material, 0 Systemic)**
    - **10 New (8 Material, 2 Systemic)**
    - **1 Transferred to Non-DoD Agency**
  - **33 Weaknesses Remaining at end of FY 2**
    - **11 Systemic**
      - **2 New**
    - **22 Material**
      - **8 New**

Internal Control = tool, plan, process that helps ensure, but does not guarantee mission accomplishment.

- **Material** = Affecting single Component
- **Systemic** = Affecting multiple Components

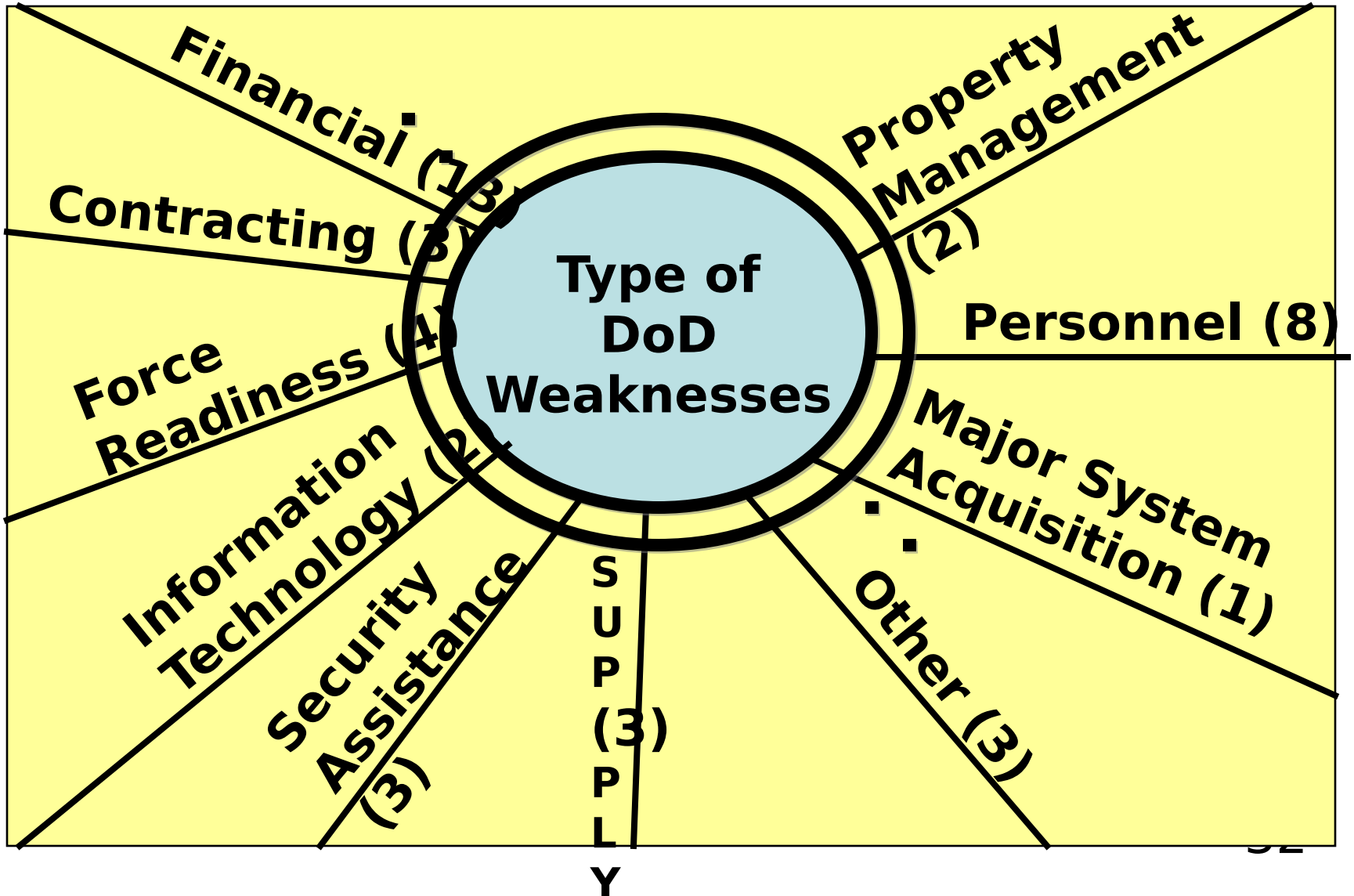
Results FY 2005 Material and Systemic Weaknesses (Continued)

- **Financial Weaknesses in Internal Controls (Section 2)**
  - **17 Weaknesses Beginning of FY 2005**
    - **8 Corrected (8 Material, 0 Systemic)**
    - **4 New (4 Material, 0 Systemic)**
  - **13 Weaknesses Remaining at end of FY 2005**
    - **5 Systemic**
    - **8 Material**
- **Financial System Nonconformance Weakness (S 4)**
  - **1 Ongoing**

Internal Control = tool, plan, process that helps ensure, but does not guarantee mission accomplishment.

- **Material** = Affecting single Component
- **Systemic** = Affecting multiple Components

DoD Weakness Areas



Scorecard Criteria for FY 2006

(BACKUP)

Statement of Assurance
~ Timely Category ~
FY 2006 Possible Scores

Blue +3 pts	• Received on or before August 25, 2006 by close of business (COB)
Green +2 pts	• Received after August 25, 2006 or by COB on September 4, 2006
Amber +1 pt	• Received after September 4, 2006 or by COB on September 6, 2006
Red -1 pt	• Received after September 6, 2006 or by COB on September 15, 2006
Black **-10 pts**	• Received after September 15, 2006

NEW!

Pts = points received or lost

Statement of Assurance
~ Format Category ~
FY 2006 Possible Scores

Blue

+3 pts

- Best in Category -- Exceptional in all aspects (Accurate, complete, easy to read and represents a good model to benchmark)

Green

+2 pts

- No revisions required and not necessary to ask for explanation from Component

AND

- Acceptable in all aspects (Accurate, complete, easy to read, and represents an acceptable model)
- Returned for correction or requested Component to clarify an aspect of the statement intent

---

Amber

+1 pt

OR

- Unsatisfactory in at least one aspect (Not accurate, not complete, not easy to read, or does not represent an acceptable model)
- Extensive changes required

OR

Red

-1 pt

- Incorrectly stated the opinion, i.e. provided an unqualified statement that should have been qualified

OR

- Statement is noncompliant in one or more aspects (Component failed to follow provided guidance in preparing statement.)

Pts = points received or lost

Statement of Assurance
~ Program Execution Category ~
FY 2006 Possible Scores

Blue

+ 3 pts

- Best in Category – Component reports at least one innovative measure **that has not been previously reported** to enhance Component-wide program execution

BUT

- Excludes any Component that scored RED in the Material Weakness Category

Green

+ 2 pts

- Statement clearly indicates that Managers' Internal Control Program (MIC) is executed at all levels (Component–wide program execution)
- Statement has limited evidence of Component-wide program execution

Amber

+1 pt

- No evidence of Component-wide program execution in statement

OR

Red

-1 pt

- Statement is over 15 days late (Late submission reflects poor program execution

Pts = points received or lost

Statement of Assurance
~ Training Category ~
FY 2006 Possible Scores

Blue + 3 pts	• Best in Category -- Component reports at least one innovative measure **that has not been previously reported** which enhances training of the Managers' Internal Control (MIC) Program Component-wide
Green + 2 pts	• Evidence in statement of Component-wide MIC Program training performed for Component managers, MIC Program coordinators, and assessable unit managers
Amber +1 pt	• Statement reflects training for different Component audiences but not all as listed for Green score
Red -1 pt	• Statement provides no evidence of Component-wide MIC Program training

Pts = points received or lost

Statement of Assurance
~ Material Weakness Reporting Activity Category ~
FY 2006 Scores

White

+5 pts

- 85% or more of weaknesses corrected on time in FY 2006 as targeted in FY 2005 Statement of Assurance. (There must be at least 2 weaknesses corrected.)

OR

- 70% or more are corrected on time and at least two weaknesses are corrected in advance of target

Purple

+4 pts

- 80% or more of weaknesses corrected on time. (There is no qualification on the number that must be corrected.)

OR

- 60% or more are corrected on time and more than one weakness corrected in advance of target

Blue

+3 pts

- 75% or more of weaknesses are corrected on time. (There is no qualification on the number that must be corrected.)

OR

- 50% or more are corrected on time and at least one weakness corrected in advance of target

Pts = points received or lost

Statement of Assurance
~ Material Weakness Reporting Activity Category ~
FY 2006 Scores (continued)

Green

+ 2 pts

- 60% or more are corrected on time

OR

- If none due for correction in FY 2006:
  - At least one new weakness reported or one weakness reported as corrected in last three years

    OR
  - Statement indicates at least two deficiencies found, that do not warrant reportin as material weaknesses and statement describes actions to resolve them (Must use format described on page 13, para s., Part I, Annual Guidance)
- 50% or more corrected on time

OR

Amber

+1 pt

- If none due for correction during FY 2006 and no new or old weaknesses in last three years, the statement of assurance must indicate at least one deficienc and actions to resolve it (Must use format on page 13, para s.)
- No weaknesses reported as new in past three years

AND

- ~~No weaknesses corrected in past three fiscal years~~

AND

Red

-1 pt

- No deficiencies with corrective actions discussed in the statement

Pts = points received or lost

Statement of Assurance
~ Material Weakness Reporting Activity Category ~
FY 2006 Scores (continued)

- One or more delinquent weakness(es) will result in a REDUCTION OF TOTAL SCORE for the Material Weakness Reporting Activity Category as follows:
  (A Component with any remaining delinquent weaknesses would receive the next lower score in the total score of this category. For example, a Component which resolved 3 of 4 or 75% of the weaknesses on time would usually receive a Blue score of 3 points. However, if that Component also had one or more delinquent weaknesses remaining open, the total score would be reduced by one color resulting in a Green score of 2 points.)

EXAMPLE

Material Weakness Reporting Activity Category

Component scores BLUE, but has one uncorrected *Delinquent Weakness*

Therefore Component Score Reduced to GREEN

Pts = points received or lost

Summary

- **Communicating the importance of internal controls:**
  - **Is one of our biggest challenges**
  - **Is the driving force for the upcoming Defense-wide awareness campaign**

- **Requirements for OMB Circular A-123 have expanded:**
  - **Appendix A – Financial Reporting**
  - **Appendix B – Government Card Program**

- **Senior leaders' roles and responsibilities:**
  - **Are being re-emphasized**

- **DoD Managers' Internal Control Program:**
  - **Has changed to meet revised OMB requirements**
  - **Is gaining in leadership's attention, emphasis and support**
  - **Has improved through use of a scorecard**